

- 14a. Suppose wages increase 2%, the cost of capital increases 3%, and a firm's product price is unchanged. What changes in the use of labor and capital would you expect the firm to make? Why?

- b. Show these changes graphically on a separate sheet of paper. Include both substitution and scale effects.

15. Suppose wages increase 2%, the cost of capital increases 3%, and the firm's product price increases by 3%. What changes in the use of labor and capital would you expect a profit-maximizing firm to make? Why?

16. Explain how the scale effect could change the outcome of 11c above (concerning an increase in the cost of capital at Araceli's Earrings).